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CHARLES ELMORE CROPLEY

IN THE

Supreme Court of the United States

OCTOBER TERM, 1945

No. 1186

LEON S. DURE, TRUSTEE OF THE GEORGIA, FLORIDA & ALABAMA RAILROAD COMPANY, AND THE GEORGIA, FLORIDA & ALABAMA RAILROAD COMPANY, DEBTOR, *Petitioner*,

v.

OTIS A. GLAZEBROOK, JR., JOSEPH FRANCE AND S. RALPH WARNKEN, CONSTITUTING THE REORGANIZATION COMMITTEE OF THE SEABOARD AIR LINE RAILWAY COMPANY, AND LEGH R. POWELL, JR., AND HENRY W. ANDERSON, AS RECEIVERS, *Respondents*.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FOURTH CIRCUIT AND BRIEF IN SUPPORT THEREOF.

JAMES H. PRICE,
Greenville, S. C.

Attorney for Petitioners.

Of Counsel
PRICE & POAG,
Masonic Temple,
Greenville, S. C.

MILLER & MILLER,
Persons Bldg.,
Macon, Ga.

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To the Honorable, the Chief Justice and Associate Justices of the Supreme Court of the United States:

The above-named Petitioners respectfully pray that a Writ of Certiorari issue to review the judgment of the United States Circuit Court of Appeals for the Fourth Circuit entered in the above entitled cause on January 23rd, 1946, dismissing Petitioner's appeal from an order and judgment of the United States District Court for the Eastern District of Virginia.

STATEMENT OF THE MATTER INVOLVED.

Because the District Judge and the Circuit Court of Appeals, in affirming his judgment and opinion in a mere per curiam order, both totally failed to apply the principles of constructive trusts, as recently announced by this Court in the

case of *Young* v. *Higbee Co.*, 65 Sup. Ct. Rep., p. 594, 89 L. ed. 578, and a long line of decisions from this Court and also decisions of the Circuit Court of Appeals for the Fourth Circuit, and because of the serious matters involved, we earnestly petition this Court to grant the writ of certiorari prayed for and fully decide the case upon its merits.

SUMMARY STATEMENT OF UNDISPUTED FACTS

The Georgia, Florida & Alabama Railroad Company, hereinafter referred to as the G.F.&A., is a Georgia railroad now running from Tallahassee, Florida, to Richland, Georgia. Until about 1942 it had a line extending from Tallahassee to Carabele, Florida, on the Gulf of Mexico coast, but this line was abandoned just at the beginning of the war. A glance at the Seaboard Air Line system map will show the strategic position occupied by this little Georgia railroad company. The G.F.&A. was chartered on July 16th, 1927, and was the successor to the Georgia, Florida & Alabama Railway Company. In the new corporation the Seaboard Air Line Railway Company was the sole owner of the common stock of 10,000 shares of no par value, which in the reorganization, in consideration of the lease hereinafter mentioned, was secured for only $1,000.00. In its reorganization, dictated and controlled by the Seaboard, 10,000 shares of first preferred stock and 5,000 shares of second preferred stock of $100 par value each, were issued. A bond issue of $1,750,000.00, secured by a first mortgage on all the properties of the G.F.&.A., was issued. At the same time the Seaboard System leased the G.F.&A. lines for 99 years at a rental of approximately $180,500.00 per annum, which guaranteed the payment of interest on the bonds and the dividends on both first and second preferred stock. The lessee was to pay all taxes and operation and maintenance expenses.

Under this lease and the ownership of all the voting stock at that time the Seaboard went into complete control of the G.F.&A. When the Seaboard Air Line Railway Company went into receivership in the United States District Court for the Eastern District of Virginia on December 23, 1930, the

Receivers of that line took over the G.F.&A. The Receivers paid the lease rental up to January 1, 1931, but since that day neither the G.F.&A. nor its Receivers or Trustee have ever received anything for the use of its lines by the Seaboard Receivers.

In about May, 1933 the Seaboard Receivers applied, at or near the same time, for orders in the Receivership Court and the Interstate Commerce Commission for the right to disaffirm the lease and abandon the operation of the G.F.&A. lines. (See Order No. 143-B of Judge Way, July 6, 1934, and I.C.C. Order, Exhibit No. 1 in Transcript of Evidence in final hearing before Judge Chestnut on June 18, 1945, all of which were offered in evidence and constituted a part of the Transcript of Record before the Circuit Court of Appeals).

The Interstate Commerce Commission after full hearing denied the petition, and thereafter the Seaboard Receivers themselves applied for the operation orders in the Virginia and Florida U. S. District Courts. A similar petition for operation orders was filed in the United States District Court of the Middle District of Georgia, where the G. F. & A. had likewise landed in receivership because of the default in the payment of the interest upon its bonds, due entirely to the breach of the lease contract by the Seaboard System.

Clearly if the Seaboard Air Line Railway Company itself had remained out of receivership, or had been returned by the Court to its corporate management, and had committed the acts later perpetrated by the Seaboard Receivers and the Reorganization Committee, the Court would never have permitted it to have taken advantage of its own wrong in defaulting on its lease obligation.

But because of these operation orders, and other facts misapplied to the law by Judge Chestnut, it is contended that no trust relationship existed between the parties in this action.

In substance the operation orders, all secured upon the petition or consent of the Seaboard Receivers, provide that the lines of the G. F. & A. would be operated by the Seaboard Re-

ceivers for the account of the G. F. & A. (Judge Akerman's Order, April 27, 1936, folio 98.) The accounting was to be in accordance with the General Formula, and the operation could cease at any time upon notice to the G. F. & A. with the approval of the Receivership Courts. It was provided that the General Formula was adopted subject to any change thereafter made by the Courts. (See Judge Deaver's Order in the U. S. District Court for the Middle District of Georgia, April 27, 1936, and similar orders of the other Courts. Folio 109.) The G. F. & A. Receivers were likewise given the right to terminate the operation upon the same notice of six months, and in the event of termination by either party an accounting should be had under the General Formula, subject to change in formulas by the Courts. The Seaboard Receivers were given a first lien upon all G. F. & A. properties for any operation losses. The Receivers were thus given the advantage of using the lines of the small Georgia corporation as an integral part of its system but without any fear or risk of any losses in the operation. The records of the Interstate Commerce Commission and of the Receivership Courts indicate that the value of the G. F. & A. properties at that time was at least $3,000,000.00. The accounts of G. F. & A. and the Seaboard Receivers were squared up, if such this maneuver could be called, to December 31, 1934, leaving the G. F. & A. with a claim of some sort for rent from January 1, 1931 to January 1, 1935, of approximately $829,000.00, which is still a mythical claim of some character, never yet decided. (See Judge Deaver's Order, folio 108, and Reports by the G.F. & A. to the Interstate Commerce Commission and the annual Seaboard Reports in evidence before Judge Chestnut, and included in the Transcript of Evidence before the Circuit Court of Appeals in this case.)

Practically all of the annual reports of the Seaboard Receivers since 1936, particularly that of 1938 offered in evidence before Judge Chestnut, contain this statement:

> "Whether or not the GF&A has any allowable claim against Seaboard Air Line Railway Company under the

lease for the period subsequent to December 23, 1930, or for any part of such period, and the extent and amount of such claim, if any, is a legal question."

The records of the Seaboard Receivership show that after many long months of investigations and hearings Special Master Taylor in his Final Report repudiated the General Formula as unfair and recommended the Kennedy Formula for all Seaboard Receivership settlements and for the Reorganization program. His report was filed under date of July 20, 1943, and his report in this respect, as well as most others, was approved by Judge Chestnut on December 13, 1943. (See Orders of Judge Chestnut and Judge Akerman in the record, Folio 34.)

The application of the Kennedy Formula to the operation of the GF&A lines by the Seaboard Receivers changed the small Georgia corporation's financial status tremendously. Both formulas were applied to the actual freight and traffic passing over the GF&A lines. Under the General Formula the line was practically a deficit line; whereas under the Kennedy Formula it was an earning line.

All the way through from December 23, 1930, the GF&A had been operated by the Seaboard Receivers as a valuable and integral part of the Seaboard System.

Immediately upon the adoption of the Kennedy Formula as the yard stick for the settlement of the accounts of the GF&A, the ownership of the bonds of that Company became a vital matter. The Special Master in his plan of reorganization had allotted the GF&A bondholders new certificates, etc. worth about $750.00 per bond. Judge Chestnut in his Order of December 13, 1943, changed this to $750.00 cash, which was the value placed by the Court itself upon the GF&A bonds. The Reorganization Committee of the Seaboard about this time had developed a plan whereby this Committee would get the approval of the Court to have the Seaboard Receivers advance sufficient funds by which the Committee or the Court would purchase the GF&A bonds at $750.00 per bond. About 90% of the 1750 bonds issued by the GF&A were available for pur-

chase through a Bondholders' Committee of the Georgia corporation.

Accordingly in the early part of 1944 the Reorganization Committee filed a petition before Judge Chestnut seeking the approval of the Court for the completion of its plan. The Special Master had recommended the appointment of the Reorganization Committee to perfect the plan of reorganization of the Seaboard's System and Judge Chestnut shortly after he had taken over the Seaboard matter after the death of Judge Way of Norfolk appointed this Committee. Of course, it had no powers other than those given by the Court, and were powerless to act without the aid and cooperation of the Seaboard Receivers.

Prior to this, in March 1943, the original holders of the first preferred stock of the GF&A, despairing of receiving anything for their stock, sold all of the 10,000 shares on the open market to W. H. B. Simpson, of Greenville and W. G. Borer, of Philadelphia, for approximately $5,000.00.

The matter of the purchase of the bonds by the Reorganization Committee came up for hearing before Judge Chestnut in Baltimore on February 8, 1944.

The record shows that shortly after acquiring the first preferred stock Mr. Simpson was elected President of the GF&A and immediately attempted to get the Seaboard Receivers to advance or loan the GF&A sufficient funds with which to buy in its bonds and retire them. It also reveals that the Reorganization Committee had planned to purchase the same bonds, or 90% thereof, at $750.00 per bond and use the bonds for full face value in the foreclosure proceedings pending in the Receivership action in the U. S. District Court for the Middle District of Georgia. Principal and past due interest as of February 8, 1944, made the bonds have a face value of slightly over $2,000.00 each.

At the hearing at Baltimore on February 8, 1944, the record shows that Mr. Simpson was present as a bondholder of the GF&A and urged the Court to purchase the bonds for the

account of the GF&A instead of for the Reorganization Committee. It further shows that Judge Chestnut demanded information as to the existence of any funds or money due to GF&A out of which he could purchase the bonds for its account. The S. A. L. Receivers were also present at the hearing on February 8th and gave their full approval and consent to the plan, and recommended the purchase of the bonds as a sound investment of Seaboard Receivership funds. They were silent as to the amount due the GF&A.

At the final hearing before Judge Chestnut on June 18, 1945, it appeared that as of February 1, 1944, the Chief Accounting Officer of the Seaboard Receivers had made a calculation as to the amount of operation profits coming to the GF&A under the Kennedy Formula and that the amount as of January 1, 1944, was approximately $1,100,000. (See testimony of Jones at pages 110 and 111 of Transcript of Testimony of June 18, 1945, F. 38). At the time of the de novo hearing on June 18, 1945, the amount had increased to $1,667,455. After the hearing on February 8, 1944, Judge Chestnut granted the petition of the Reorganization Committee and refused the request of Mr. Simpson to purchase the bonds for the account of the GF&A, and passed Order R-1 on that date. This Order authorized the purchase of the bonds at $750.00 per bond and directed the Seaboard Receivers to advance the necessary funds for this purpose. The Reorganization Committee not only did not furnish the money but by the provisions of Section F of the Order were expressly declared not to be obligated in any respect for the repayment of the money advanced by the Seaboard Receivers.

The foreclosure proceedings in Georgia were immediately revived after a dormant session of six or eight years and it is admitted that the bonds were to be used against the GF&A at their full value.

The GF&A in July 1944 filed a petition for reorganization under Sec. 77 in the U. S. District Court for the Middle District of Georgia.

The Trustee of the GF&A appointed by the Bankrupt Court

sought by petition to bring the Seaboard Receivers and the Reorganization Committee into the Georgia Court for the purpose of accounting and to decide the ownership of the bonds. The Respondents challenged the jurisdiction of the Georgia Court and the late Judge Lovett, of Savannah, sustained their plea to the jurisdiction of the Court.

As neither the GF&A, whose corporate status has been preserved and kept alive, nor its Receivers, were parties to the hearing on February 8, 1944, the Reorganization Committee realized that there would remain a serious question as to its title to the bonds and, on March 14, 1945, petitioned Judge Chestnut to reopen the matter and hear the case de novo (See Mr. Adkins' statement to the effect that the hearing was de novo, page 9, Transcript of Evidence of the hearing on June 18, 1945, which was a part of the Transcript of Record before the Circuit Court of Appeals).

After full hearing Judge Chestnut reaffirmed his former order and filed a lengthy opinion in which he said, among other things: "I do not think the resulting relationship (created by the operation orders) constituted a trust of any character." (F. 43)

THE ISSUE

So the issue is clear. Was there such a trust or fiduciary relation between the Seaboard Receivers and G.F.&A. as to prohibit them from directly or indirectly acquiring title to the bonds in question, at about one-third of the face value, with funds partly built up by the GF&A as an integral part of the Seaboard System and then using the bonds at full value against the GF&A in order to obtain possession of its properties?

If the fiduciary or trust relationship existed then this Writ should be granted so that this Court, upon a full inquiry, could decide whether the Circuit Court of Appeal's decision should be reversed. If a trust or fiduciary relationship did not so exist, our petition should be denied.

OPINION BELOW

The per curiam opinion of the Circuit Court of Appeals, reported in 152 Fed. (2nd) 756 appears in the printed record at Folio 126. The opinion of Judge Chestnut thereby adopted is reported in 62 Fed. Supp. at 207, and appears in the record at Folios 15 and 27.

JURISDICTION

The jurisdiction of the Court is invoked under Sec. 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925 (U. S. Code Annotated, Title 28 Sec. 347 (a)).

REASONS RELIED ON FOR THE ALLOWANCE OF THE WRIT

1. The decision of the Circuit Court of Appeals ignores the decision of this Court in the case of *Young* v. *Higbee Co.*, 65 S. Ct. Rep. 594; 89 L. ed. 578 and in not declaring that a constructive trust existed for the benefit and protection of the GF&A and its stockholders, the decision appealed from is contrary to that opinion.

2. The declaration of a constructive trust by a Court of Equity in a proceeding properly before it is a matter of law, if the essential facts are without dispute. Here the main facts are admitted and both the District Court and the Circuit Court have erred as a matter of law in failing to apply the facts to the law and declaring the existence of a constructive trust in favor of the GF&A and its stockholders. As the lower court has erred in this respect, we ask this Court to grant the writ of certiorari and later to declare the trust in a hearing upon the merits.

3. The decision below failed to apply the principles of equity as to the duty of one in a trust or fiduciary relationship with another as applied in a long line of decisions of this Court, such as *Buffum* v. *Barcelous Co.*, 289 U. S. 277, wherein it was held that "the standard of duty is no different whether the trust to be enforced is actual or constructive. The im-

plication of a trust is the implication of every duty proper to a trust."

4. The decision below was perhaps influenced by the sympathy of the lower court in the plan to perfect the reorganiation of the Seaboard Air Line Railway System. The Receivers and the Reorganization Committee were arms of the Court and these officers of the Court conceived and recommended the plan to purchase the bonds of the GF&A, without considering the rights and interests of the much smaller corporation and the lower court lost sight of the fact that "equity has its distinctive standards of fidelity and honor, higher at times than the standards of the market place."

Buffum v. *Barcelous Co.*, supra.

5. The decision below makes it impossible for the GF&A to work out any tenable or basicly sound reorganization plan. As of the date of the hearing before Judge Chestnut it had an asset of $1,667,000.00 in net earnings due it from the Seaboard Receivers, which the Circuit Court of Appeals' decision makes it impossible for the GF&A to use. By declaring, as it does, that "the title to these GF&A bonds is vested in the Seaboard Reorganization Committee free of any equity, claim or lien" in favor of the GF&A or its trustee, the decision makes it possible for the Reorganization Committee to file a claim against the bankrupt Company for approximately $4,000,000.00 and enforce it, when they only used $1,169,250.00 of Receivership funds in acquiring the bonds.

6. The decision below somewhat degenerates the issue to a question as to the superior equities between the Seaboard lien creditors and the GF&A and its stockholders, instead of holding the inquiry to the sole point involved, viz, the existence or non-existence of a trust or fiduciary relationship between the parties.

7. The decision below failed to follow the decisions of this Court and its own decisions to the effect that when the trust or fiduciary relationship is found to exist, the inquiry should stop and the transaction complained of should be set aside.

Trice v. *Comstock*, 121 Fed. 620. cited by the Circuit Court of Appeals for the Fourth Circuit as authority for its decision in the case of *Finefrock* v. *Kenova Mine Car Co.*, 22 Fed. (2nd) 627.

WHEREFORE, the Petitioners pray that a writ of certiorari issue to review the judgment of the United States Circuit Court of Appeals for the Fourth Circuit entered in this case on January 23, 1946.

JAMES H. PRICE,
Attorney for Petitioners

Of Counsel

PRICE & POAG,

Masonic Temple
Greenville, S. C.

MILLER & MILLER,

Persons Bldg.,
Macon, Ga.